

**LEGISLATIVE SERVICES AGENCY
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FISCAL IMPACT STATEMENT

LS 6269

BILL NUMBER: SB 409

NOTE PREPARED: Jan 2, 2012

BILL AMENDED:

SUBJECT: Income Tax Exemption for Military Pay.

FIRST AUTHOR: Sen. Waltz

FIRST SPONSOR:

BILL STATUS: As Introduced

FUNDS AFFECTED: X GENERAL
DEDICATED
FEDERAL

IMPACT: State & Local

Summary of Legislation: The bill exempts military pay earned by members of an active component of the United States armed forces from the individual income tax. (Current law exempts from the individual income tax the military pay earned by members of the National Guard and reserve components of the United States armed forces while serving on active duty.)

Effective Date: January 1, 2012 (retroactive).

Explanation of State Expenditures: *Department of State Revenue (DOR):* The DOR would incur some administrative expenses relating to the revision of tax forms, instructions, and computer programs to reflect the deduction change. The DOR's current level of resources should be sufficient to implement this change.

Explanation of State Revenues: *Summary* - The bill increases the adjusted gross income (AGI) deduction for military service pay earned by individuals who are members of an active component of the U.S. armed forces. The deduction would be increased from a maximum of \$5,000 to a full deduction for military service pay earned by such individuals. It is estimated that the revenue loss from this change could potentially total \$13.7 M in FY 2013. The revenue loss could grow by 2.5% annually based on recent annual growth in active duty pay. This estimate is based on a 2011 Census by the U.S. Department of Defense (DOD) of active duty personnel reporting Indiana as their state of legal residence and annualized pay to those individuals. The estimate assumes that these individuals are already claiming a \$5,000 deduction and is to account for Armed Forces Reserve and National Guard personnel who currently claim the full deduction for active duty pay.

Background Information - Current statute provides an AGI deduction for the first \$5,000 of income earned by an individual for his or her service in an active or reserve component of the U.S. armed forces, including the National Guard. The \$5,000 deduction also applies to military retirement income or survivor's benefits received by a taxpayer who is 60 years old or older. Also, current statute provides a full deduction for active duty pay earned by members of the Armed Forces Reserve or National Guard in lieu of the deduction for military service income described above. (Note: Combat pay is already excluded from federal gross income and, as a result, is excluded from Indiana AGI.)

In 2011, the DOD reported that 20,201 individuals on active duty during the year reported that Indiana was their state of legal residence. These individuals received an estimated \$510.4 M in active duty pay during the year. Based on 2009 Indiana tax return data, its estimated that almost 1,672 of these individuals were Armed Forces Reserve or National Guard members who received an estimated \$26.1 M in active duty pay. and, thus, already eligible for a full deduction under current statute. Assuming the remaining 18,529 active duty personnel currently claim the current \$5,000 deduction, the additional deductible pay under the bill would total \$404.2 M.

Explanation of Local Expenditures:

Explanation of Local Revenues: Because the deduction increase will decrease taxable income, counties imposing local option income taxes could potentially experience a decrease in revenue from these taxes. Based on the current average LOIT rate of about 1.4%, the additional revenue loss due to the increased deduction could total as much as \$5.7 M. This could be lower depending on factors such as marital status and where the individual is stationed.

State Agencies Affected:

Local Agencies Affected:

Information Sources: U.S. Department of Defense, Defense Manpower Data Center. OFMA Income Tax Return databases.

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